

DEPARTMENT OF STATE REVENUE

01-20160070.LOF
10-20150525.LOF
04-20150526.LOF**Letter of Findings: 01-20160070; 10-20150525; 04-20150526****Gross Retail Tax
Food and Beverage Tax
Individual Income Tax
For the Years 2012, 2013, and 2014**

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Indiana Gas Station/Convenience Store failed to meet its burden of establishing that an audit assessment of sales, food and beverage, and its Partners' individual income tax was incorrect; the audit correctly accounted for the Gas Station/Convenience's lottery sales. In the absence of complete and accurate business records, the assessment of food and beverage and income tax was based on the best information available the Department.

ISSUES**I. Gross Retail Tax - Lottery Sales.**

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-9-3; IC § 6-8.1-5-1(b); IC § 6-8.1-5-1(c); IC § 6-8.1-5-4(a); Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); [45 IAC 15-5-1](#).

Taxpayer argues that the method by which the Department's audit accounted for its lottery sales inflated the amount of its retail sales income subject to tax.

II. Food and Beverage Tax - Calculation.

Authority: IC § 6-9-21-5; IC § 6-9-21-6; IC § 6-8.1-5-1(c); Commissioner's Directive 30 (October 1, 2013).

Taxpayer maintains that - similar to the questions raised in Part I above - the audit's calculation of its sales inflated the amount of its retail income subject to Food and Beverage Tax.

III. Indiana Individual Income Tax - Calculation.

Authority: IC § 6-3-4-11; IC § 6-3-4-11(a); IC § 6-8.1-5-1(c); IC § 6-8.1-5-4(a).

Taxpayer(s) state that the Department's audit of their business income was incorrect resulting in a misstatement of the amount of income subject to individual income tax.

STATEMENT OF FACTS

Taxpayer is an Indiana business entity which operates a combination gas station and convenience store. Taxpayer sells gasoline, tobacco products, grocery items, newspapers, prepaid phone cards, lottery tickets, and the like.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns.

The audit resulted in the assessment of additional sales, food and beverage, and the partners' personal income tax.

Taxpayer disagreed with the assessments and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Letter of Findings results.

I. Gross Retail Tax - Lottery Sales.

DISCUSSION

Taxpayer disagrees with the assessment of additional sales tax on three grounds: (1) Taxpayer maintains that the audit did not properly account for exempt lottery sales; (2) Taxpayer maintains that the audit understated the amount of its exempt sales; (3) Taxpayer maintains that the audit did not properly account for the amount of sales tax it collected and forwarded the Department.

A. Audit Results.

The Department's audit requested copies of Taxpayer's complete business records in order to determine if sales tax had been properly assessed and collected. The request was only partially successful. The Department obtained federal and state income returns, original sales tax returns, vendor invoices, and bank statements.

The Department was unsuccessful in obtaining "daily z-tapes" (cash register receipts) as records of Taxpayer's daily in-store sales. Taxpayer explained that the z-tapes were unavailable because the z-tapes had been stored in an outbuilding which suffered flood damage. The z-tapes for the period following the flood were unavailable because the tapes were printed on thermal paper which - according to Taxpayer - had faded to illegibility.

Because daily sales records were unavailable, the "audit calculated sales based on the records the [T]axpayer supplied."

The monthly bank statements deposits were totaled. The audit deducted the direct deposits from [gasoline vendor], these payments are the credit card sales made at the [T]axpayer's location less any unpaid fuel purchases. The audit also deducted the EBT deposits, [redacted] direct deposits, sales tax remitted to the Department, other income and [cigarette vendor] direct deposits.

The audit found that "cash payouts are routinely made at the convenience store for deliveries made at the store." Taxpayer made direct cash payouts to its soft drink vendors, local dairy, and to the newspaper carrier. To account for these direct cash payments, the audit "multiplied the bank deposits by 30 percent."

In its subsequent report, the audit recognized that "[c]onvenience stores have exempt sales for items such as newspapers, food stamp purchases, and exempt food items." On its originally filed sales tax returns, Taxpayer reported that 55 percent of the in-store sales were exempt from sales tax an amount which the audit concluded was "excessively high for a convenience store."

According to the audit report:

Industry averages for this type of business have exempt sales of 5 to 10[percent]. The audit [reviewed] the 2012 vendor invoices . . . and calculated that 7.5[percent] of the purchases were for items exempt from sales tax. The audit deducted 7.5[percent] of the total in-store sales per audit to account for the sales of exempt items. The audit then deducted the in-store taxable sales per the [T]axpayer's filed ST-103MP's.

In addition, the audit also reviewed available records of Taxpayer's tobacco sales. A review of Taxpayer's 2012 purchases found that 87 percent of Taxpayer's total in-store purchases were for tobacco products. The audit concluded that "[g]iven that fact, the [T]axpayer's taxable sales should be much higher than reported." The audit noted that "[t]he tobacco products purchases alone are greater than the [T]axpayers reported taxable sales and this does not include any soft drinks or any other taxable products."

B. Taxpayer's Response.

Taxpayer states its "main issue" is the audit's accounting of exempt lottery sales. Taxpayer maintains that lottery sales should not be included as part of its "gross sales, neither are they a part of the cost of goods sold." Taxpayer proposes reverting to a previous audit worksheet as the proper method of reporting its taxable sales.

Taxpayer also argues that more than 7.5 percent of its sales are exempt. Instead Taxpayer explains that "many factors can impact the amount of exempt sales" including "store location and the demographics of neighborhoods around the store."

Finally, Taxpayer argues that the audit failed to credit it with the correct amount of sales tax paid during the audit period. The audit credited Taxpayer with having paid approximately \$81,000 in sales tax over the three-year audit period. Taxpayer states that it actually paid approximately \$219,000 in sales tax during that period and presented "INTax" records to support that assertion.

C. Hearing Analysis.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014). Thus, interpretations of Indiana tax law contained within this decision, as well as the preceding audit, are entitled to deference.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A retail merchant - such as Taxpayer - is required to "collect the tax as agent for the state." IC § 6-2.5-2-1(b). The retail merchant "holds those taxes in trust for the state and is personally liable for the payment of those taxes" IC § 6-2.5-9-3.

As a business conducting retail transactions and collecting sales tax on behalf of the state, Taxpayer was required to maintain complete and accurate financial records including register receipts. "Every person subject to a listed tax must keep books and records so that the [D]epartment can determine the amount, if any, of the person's liability for that tax by reviewing those books and records." IC § 6-8.1-5-4(a). The "records" referenced "include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks." *Id.*

In the absence of accurate or complete records, Indiana law requires that the Department issue a proposed assessment based on the best information the Department can obtain. "If the [D]epartment reasonably believes that a person has not reported the proper amount of tax due, the [D]epartment shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the [D]epartment." IC § 6-8.1-5-1(b). See also [45 IAC 15-5-1](#).

The first issue is whether, in issuing its assessment, the audit correctly accounted for exempt lottery sales. Taxpayer states that its lottery sales are not part of its gross sales and should not be used in calculating receipts subject to sales tax. Taxpayer cites to a preliminary audit worksheet which accounted for those lottery sales differently from the calculation contained on the final audit worksheet.

The Department agrees that lottery sales are not subject to sales tax. However, Taxpayer misunderstands the difference between the calculation set out in the preliminary worksheet and the calculation set out in the final worksheet.

Because Taxpayer did not have complete sales records, the Department was required to reconstruct the total amount of Taxpayer's in-store sales. As part of that calculation, the audit was required to account for the fact that Taxpayer routinely made direct cash payment to its vendors. In other words, Taxpayer took cash from its register on a daily basis to pay certain of its vendors. The audit multiplied Taxpayer's bank deposits and other receipts by 30 percent and then added that 30 percent to those other receipts.

In the preliminary worksheet, lottery sales are not accounted for in the 30 percent calculation; in the final worksheet, that omission is corrected and the audit includes lottery sales in the 30 percent calculation. In other words, was the audit correct in concluding that lottery receipts constituted of portion of Taxpayer's cash-on-hand paid out to its soft drink, dairy, and newspaper vendors on a daily basis from its cash register? The answer is "yes." The Department finds no fault in the audit's calculation because money received from selling lottery tickets

would have found its way into Taxpayer's register receipts and would have been used - in part - to pay Taxpayer's vendors.

The second issue is whether the Department's audit overstated the amount of Taxpayer's sales subject to tax. Of course, it is not possible to determine with certainty the amount of taxable sales or the amount of exempt sales. Whether through Taxpayer's negligence, an act of God, or the vagaries of fading thermal paper, records of Taxpayer's daily sales are not available. Nonetheless, it was Taxpayer's responsibility to keep those records and make them available for review. Correspondingly, it was the Department's responsibility to issue an assessment based on the best information available.

The Department does not agree that - based in part on vendor records - that Taxpayer has met its burden of establishing that the assessment was "wrong." Those vendor records establish that much of what Taxpayer bought for sale in its store were items which were subject to sales tax. Simply reviewing Taxpayer's tobacco product purchases for 2012, indicates that the sales tax on those items alone would exceed the amount of sales tax Taxpayer reported that year. Taxpayer has provided no support for its position that more than one-half of Taxpayer's sales were exempt from sales tax.

The third issue is whether the Department's audit correctly credited Taxpayer for the amount of sales tax collected during this period. The Department's audit reviewed Taxpayer's sales tax returns (ST-103MP) and credited Taxpayer for having paid approximately \$81,000 in sales tax over the three-year period. Taxpayer provided "INTax records" which, on their face, indicate that Taxpayer paid \$219,000 in sales tax during that period.

On its INTax returns filed for 2012, 2013, and a portion of 2014, Taxpayer reported total sales included "pre-paid" gasoline use tax. In preparing the audit work papers, the Department's audit gave Taxpayer credit for sales tax paid on its in-store sales but not for the prepaid sales tax. Although the prepaid sales tax was included on the amount reported by means of INTax, the audit correctly credited Taxpayer only the amount of tax collected on non-gasoline sales.

FINDING

Taxpayer's protest is respectfully denied.

II. Food and Beverage Tax - Calculation.

DISCUSSION

The Department's audit found that Taxpayer was selling items at its store which were subject to food and beverage tax. As explained in the audit report, Taxpayer sold food to its customers "in a heated state" and also sold fountain drinks, "slushies," coffee, and hot drinks. However, Taxpayer had not registered to collect and remit food and beverage tax.

The Department's audit report cited to Commissioner's Directive 30 (October 1, 2013), 20131127 Ind. Reg. 045130521NRA, as authority for its determination that Taxpayer was selling items subject to the tax. The Directive states in part:

The food and beverage tax applies to any transaction in which food or beverage is furnished, prepared, or served by a retail merchant for consumption at a location or on equipment provided by the retail merchant in a county or municipality that adopts the tax.

"For consumption at a location or on equipment provided by the retail merchant" includes transactions in which food or beverage is (1) served by a retail merchant off the merchant's premises, (2) sold in a heated state or heated by a retail merchant, (3) made of two or more food ingredients, mixed or combined by a retail merchant for sale as a single item (other than food that is only cut, repackaged, or pasteurized by the seller and eggs, fish, meat, poultry, and foods containing these raw animal foods requiring cooking by the consumer as recommended by the federal Food and Drug Administration), or (4) food sold with eating utensils provided by a retail merchant, including plates, knives, forks, spoons, glasses, cups, napkins, or straws. A container or package used to transport the food is not considered a plate.

IC § 6-9-21-5 imposes a one percent food and beverage tax on Delaware county vendors.

The county food and beverage tax imposed on a food or beverage transaction described in section 4 of this

chapter equals one percent (1[percent]) of the gross retail income received by the merchant from the transaction. For purposes of this chapter, the gross retail income received by the retail merchant from such a transaction does not include the amount of tax imposed on the transaction under [IC 6-2.5](#).

Delaware County's food and beverage tax is imposed, paid, and collected in the same manner that the state gross retail tax is imposed, paid, and collected under [IC 6-2.5](#). IC § 6-9-21-6. "However, the return to be filed for the payment of the taxes may be made on separate returns or may be combined with the return filed for the payment of the state gross retail tax, as prescribed by the department of state revenue." Id.

A retail merchant who sells taxable food items collects the tax on behalf of the locality and remits the tax to the Department; in that sense the retail merchant is a tax collector. As a collector of the food and beverage tax, a retail merchant is subject to the same collection requirements that apply to the collection of sales tax.

As noted in Part I above, Taxpayer did not have accurate and complete records of its daily sales. In the absence of those records, the Department's audit calculated the tax based on information found at the "National Association of Convenience Stores" website. According to the audit report, "A search of [the Association's] media releases revealed that 18[percent] of 2013 sales were foodservice (prepared and commissary food; hot, cold and dispensed beverages)."

Other than disagreeing with assessment, Taxpayer has provided nothing which would bring into question the audit's assessment of this tax. Taxpayer has not met its burden under IC § 6-8.1-5-1(c) of establishing that the proposed assessment of food and beverage tax was wrong.

FINDING

Taxpayer's protest is respectfully denied.

III. Indiana Individual Income Tax - Calculation.

DISCUSSION

In Parts I and II, this Letter of Findings addresses assessments of sales and food and beverage tax issued against the Indiana business entity. This section of the "Letter of Findings," addresses the additional individual income tax section assessed the partners/ owners of that business entity.

The audit cited to IC § 6-3-4-11 authority for its position that - although the business entity was not subject to income tax - the partners ("Taxpayers") - were. The statute provides in part:

A partnership as such shall not be subject to the adjusted gross income tax imposed by [IC 6-3-1](#) through [IC 6-3-7](#). Persons or corporations carrying on business as partners shall be liable for the adjusted gross income tax only in their separate or individual capacities. In determining each partner's adjusted gross income, such partner shall take into account his or its distributive share of the adjustments provided for in [IC 6-3-1-3.5](#).

IC § 6-3-4-11(a) (Emphasis added).

The income tax audit noted that the Department's audit review of the business entity "resulted in an increase in sales and therefore an increase in additional income."

In objecting to the additional income tax assessment, the Taxpayers (partners) revert to the same objections set out in Parts I and II above. Taxpayer makes no other argument then to again point out that the audit purportedly overstated the amount of the business entity's receipts. However, the Department's response here is identical. Taxpayers were required under the law to prepare and maintain "books and records so that the Department can determine . . . liability for the tax . . ." IC § 6-8.1-5-4(a). In the absence of those records the Department was obligated to make a proposed assessment of the relevant tax. Id.

As in Parts I and II above, Taxpayers have not met their burden of establishing that the proposed assessment of additional income tax was "wrong." IC § 6-8.1-5-1(c).

FINDING

Taxpayers' protest is respectfully denied.

SUMMARY

Taxpayers' objections to the sales, food and beverage, and income tax assessments are denied.

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